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INFO RUCNASE/ASEAN MEMBER COLLECTIVE  
RUEHBY/AMEMBASSY CANBERRA 1597  
RUEHBJ/AMEMBASSY BEIJING 2081  
RUEHKA/AMEMBASSY DHAKA 5026  
RUEHNE/AMEMBASSY NEW DELHI 5081  
RUEHUL/AMEMBASSY SEOUL 8679  
RUEHKO/AMEMBASSY TOKYO 6248  
RUEHCN/AMCONSUL CHENGDU 1619  
RUEHCHI/AMCONSUL CHIANG MAI 1893  
RUEHCI/AMCONSUL KOLKATA 0467  
RUEAIIA/CIA WASHDC  
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RUEHGV/USMISSION GENEVA 4098  
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C O N F I D E N T I A L SECTION 01 OF 04 RANGOON 000836

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TAGS: EFIN ECON PGOV IMF BM

SUBJECT: BURMESE PRIVATE SECTOR REPS DISCUSS ECONOMY WITH IMF

REF: A. RANGOON 698  
1B. RANGOON 663  
1C. RANGOON 596

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Classified By: Economic Officer Samantha A. Carl-Yoder for Reasons 1.4 (b and d).

Summary

11. (C) During a roundtable discussion between the IMF Article IV Consultation team and Burmese private sector business and economic observers, participants discussed problems in the banking industry, the use of informal channels for fund transfers and capital financing, the problems associated with Burma's high inflation, and the need for exchange rate unification. Participants confirmed the IMF's assertion that Cyclone Nargis had a much smaller economic impact on Burma than previously expected. The IMF team plans to limit recommendations to the GOB to one or two key reforms, rather than a slate of changes as proposed in the past. The IMF team agreed that Burma had fallen behind its neighbors due to economic mismanagement. End Summary.

12. (C) The DCM on October 24 hosted a lively roundtable discussion for the visiting IMF Article IV team with local bankers and private economic consultants. Team leader Ranil Salgado, IMF Deputy Division Chief for Asia and the Pacific, opened the meeting by noting that in the past, IMF Article IV teams had proposed to the GOB a package of necessary economic reforms - with little success. As a result, this year the IMF will recommend one or two key reforms, which may be more realistic to implement. Salgado and his team emphasized that

while the GOB has achieved some positive results in the past few years, including higher tax revenues and liberalization of the agriculture sector, problems such as an inefficient multiple exchange rate system, high government expenditures, high inflation, and a poorly developed banking sector remain.

#### Need to Tackle Inflation

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¶3. (C) U Maw Than, former Rector of the Myanmar Institute of Economics, noted that Burma's high inflation rate, estimated at 40 percent, is the main reason for the lack of economic growth and the proliferation of informal financial mechanisms. The GOB continues to finance its deficit by printing money, and people are unwilling to deposit money into banks because the 17 percent interest rate does not come close to covering the rise in prices. Inflationary pressure in Burma will continue to increase unless the government reduces deficit spending, stops printing money at will, and increases revenue collection. Several other participants echoed U Maw Than's concerns about the negative impacts of persistent high inflation.

¶4. (C) IMF Senior Economist Tubagus Feridhanusetyawan noted that according to Burma's Central Statistical Office, inflation has remained steady at 28 percent (as of June 2008), although Cyclone Nargis caused a slight increase to 31 percent in May. SGS Consultant U Kyaw Tin commented that this rate was too low, but that the general trend is accurate. The economic effects of Cyclone Nargis have been less than previously expected; other rice growing regions have made up the rice shortfalls expected from the Irrawaddy

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Delta, foreign assistance has helped cyclone victims regain some of their livelihoods, and inflation increased modestly immediately after Nargis but has returned to pre-Cyclone levels, he stated.

#### Financial Sector Difficulties Abound

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¶5. (C) Several Burmese participants complained to the IMF about the inefficiencies of the financial sector, particularly the highly segmented financial market and restrictions on private bank activity. Since 2003, private banks have been unable to open bank branches, must restrict deposits, and do little lending. The Central Bank, private consultant U Soe Win noted, lacks operational independence and the technical capacity to make financial sector recommendations to the government. He requested that the IMF again make recommendations regarding the need to improve financial operations, level the playing field between state and private banks, and allow private banks to "act like banks." The Burmese banking sector, he stressed, must be allowed to take on and manage risks. He also noted that the GOB should also clearly define the role of state-owned banks, ensure fair competition between private and state-owned banks, allow foreign banks to operate in Burma, and promote Central Bank independence.

¶6. (C) In the absence of a strong banking sector, all participants agreed, Burmese citizens are forced to turn to the informal sector for financial transactions and access to credit. Burmese Economist Winston Set Aung confirmed that most people use informal channels, known as the hundi/hawala system, to transfer money (Ref A) from outside the country. Within Burma, the informal sector also provides loans, with interest rates ranging from three to twenty percent, depending on available collateral, he noted. Seventy percent of all borrowing in Burma occurs through informal channels, either because banks are unable to offer loans or because Burmese lack the collateral necessary to secure a bank loan. Participants confirmed Salgado's observation that formal credit is rationed in Burma, so only those who have access to

formal lending, i.e. cronies and regime relatives, can benefit from current financial sector regulations.

¶7. (C) IMF Economist Feridhanusetyawan inquired about whether the GOB has ever issued bonds to raise money and provide an outlet for domestic savings. SGS Consultant U Kyaw Tin pointed out that the Burmese people lack faith in the banking and financial systems, and that any bond would have to offer an interest rate high enough to overcome Burma's high inflation rate, i.e., greater than 40 percent. Several attendees noted that those Burmese who have money to save prefer to do so by either buying U.S. dollars or gold, speculating in forward markets (e.g., for rice and other agricultural commodities), or by buying property. As one put it, as a result of the pressure to earn returns that will keep up with inflation, "We have become a nation of gamblers." The majority of Burmese, however, are unable to save money; anything they do have, they keep in their homes rather than in banks.

#### Exchange Rate Discrepancies

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¶8. (C) The IMF team also inquired about the impact of Burma's multiple exchange rate regime, which establishes

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different unofficial exchange rates depending upon the transaction. (Note: While the official rate is 6 kyat/1 USD, the black market rate is 1270 kyat/1 USD. Additionally, there are six other exchange rates where the kyat/USD rate varies by transaction. Please see Rangoon 137 for a complete description.) For years, the GOB has been reluctant to make any adjustments in the exchange rate system; Salgado commented that this year was not likely to be any different. U Soe Win, a former Central Bank Governor, commented that the GOB should have unified rates more than 10 years ago, but has been afraid that it would increase prices and lead to public unrest. The participants agreed that almost all Burmese use the black market exchange rate, and concluded that the official rate is only useful for the regime to exaggerate its national income accounts.

¶9. (C) Feridhanusetyawan confirmed that the GOB doubled the amount of FEC in the market, from 20 to 40 million, after Cyclone Nargis, which accounted for a large but temporary FEC/U.S. dollar exchange rate discrepancy (Refs B and C). He inquired about whether businessmen engaged in arbitrage to earn money on the FEC/U.S. dollar spread. Participants noted that some businesspeople with cash in hand had exploited the differential, but most did not. Feridhanusetyawan commented that the GOB - through state-owned enterprises such as Myanmar Economic Holdings Ltd. (MEHL) or Myanmar Economic Corporation (MEC) - could have profited handsomely from the exchange rate discrepancy. U Soe Win noted that most GOB officials do not have the economic sophistication to realize the opportunity; moreover military-owned operations such as MEHL or MEC follow orders rather than make independent economic decisions.

#### Little Access to Data

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¶10. (C) At the end of the discussion, the businessmen praised the IMF as one of the few organizations that can obtain economic data from the GOB. One of the participants observed that while select economic information is available on the internet, the GOB closely controls all fiscal data. Budget information, which is printed annually, is not widely distributed and many Burmese doubt the quality of the statistics in any event. Salgado noted that officials have been very forthcoming with statistics, although transmission is often delayed. He also explained that the IMF Article IV consultation enables different branches of the GOB, including the Central Bank, to see financial data to which they otherwise have no access.

Comment

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¶11. (C) The IMF Article IV team appears to be taking a rational approach in trying to understand Burma's economic problems, though most of Burma's economic policies defy logic. We constantly hear complaints about how difficult it is to do business here -- one must be connected, willing to pay bribes, creative with regard to informal financing, and tolerant of the inefficiencies and uncertainties concerning commercial regulations. The roundtable event provided the IMF with the opportunity to hear from those directly affected by the GOB's poor economic policies. The IMF team recognizes clearly that economic growth in Burma requires macroeconomic reforms. From our perspective, its plan this year to focus on one or two important (and political feasible) reforms,

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rather than a laundry list of policy changes, makes sense. The IMF members will provide an outbrief to the Embassy on their meetings with GOB officials before departing Burma on November 5.

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